1999 Legislative Guide to Washington State Property Taxes

Prepared by the Senate Ways and Means Committee staff

Table of Contents

Introduction

A *Legislative Guide to Washington State Property Taxes* is offered as a resource to members of the Senate, their staff, and other interested persons to provide an overview of the property tax system in this state. It describes the evolution and characteristics of our property tax structure, provides comparative and historical analyses, and outlines the various policy issues and changes that are under consideration by various parties with a stake in the current tax system.

The *Legislative Guide to Washington State Property Taxes* was developed by the Senate Ways and Means Committee staff (within Senate Committee Services) to provide answers to many of the typical questions regarding property taxes. These questions range from general requests for a summary of the overall property tax system to very specific inquiries regarding technical aspects of administering the tax. Over the past several legislative sessions, numerous proposals to provide property tax relief or reforms have been considered by the Legislature including Referendum 47 which was passed in November 1997 (see page 18 for a complete discussion).

This *Legislative Guide to Washington State Property Taxes* is a summary of our property tax system intended to assist its readers in understanding basic terminology and gaining a historical and analytical perspective with which to evaluate potential reforms. Staff of the Senate Ways and Means Committee have also developed a *Washington State Property Tax Manual* that provides a more in-depth look at property taxes. It is much more comprehensive and technical, requiring a basic understanding of the property tax system and terminology.

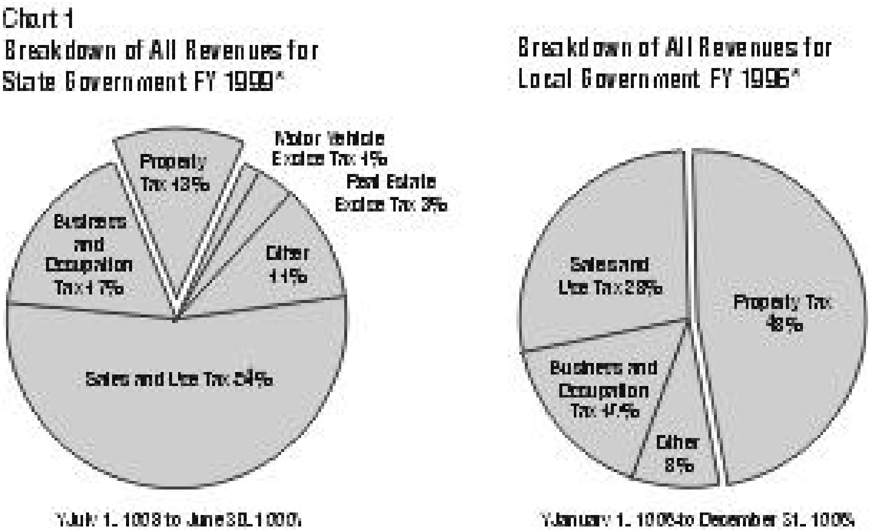
The *Washington State Property Tax Manual* was developed as a resource document and is available upon request.

Questions concerning this report or requests for the *Washington State Property Tax Manual* should be addressed to the staff of the Senate Ways and Means Committee, 300 John A. Cherberg Building, Olympia, Washington 98504. Telephone: (360) 786-7715.

How Much Money Does the Property Tax Generate and How is it Spent?

In 1998, Washington State taxpayers paid a total of $4.7 billion in property taxes to local governments, state government, and school districts. Property taxes are the single largest source of revenue for local governments, generating about $1.5 billion per year, approximately 48 percent of local government tax revenues. The property tax is the third largest source of revenue to the state General Fund, generating approximately $1.2 billion in FY 1998 or about 12 percent of General Fund revenue. The remaining $2.0 billion is distributed to local school districts for maintenance and operations (M&O) or capital construction.

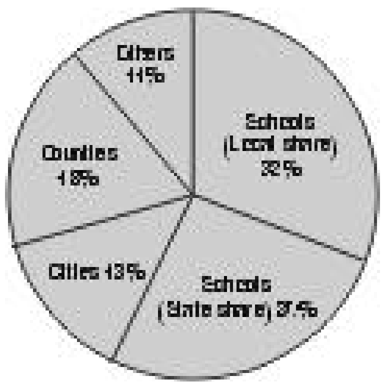
Chart 1 shows the breakdown of all revenues for state and local government by source of revenue.



Local government consists of hundreds of separate taxing districts across the state. In addition to the state (a single taxing district for purposes of collecting the state levy), there are 39 counties, 271 cities and towns, 381 fire districts, 139 emergency medical service (EMS) districts, 73 ports, and 15 library districts. Chart 2 breaks down the $4.7 billion in property taxes collected in 1998 by the type of taxing district.

Collectively, school districts receive 32 percent of the revenue from property taxes, the largest portion of the total. The state receives the largest share for any single taxing district, 26 percent. The state's share is distributed entirely to public schools, as will be discussed later. In total, 57 percent of all property tax revenue is collected in support of K-12 education. The proportions displayed in Chart 2 represent the distribution of taxes collected from the "average" individual taxpayer in the state.

Chart 2
Distribution of Property Taxes - CY 1998



What Property is Taxable?

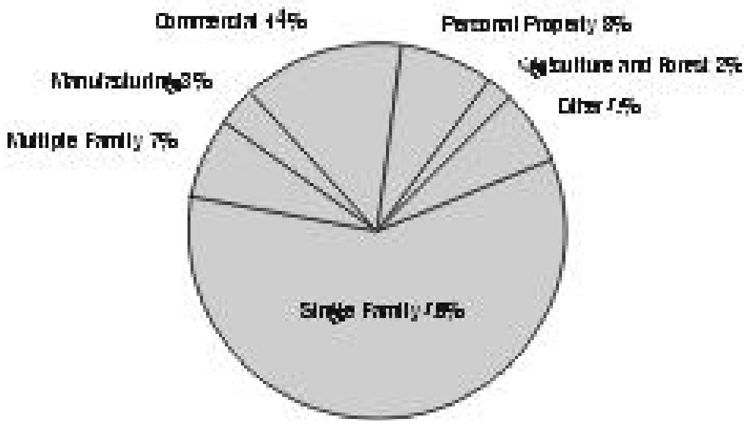
The 14th Amendment to the State Constitution defines property as everything that can be owned, whether tangible or intangible. The property tax is applied annually to the assessed value of all property unless it is specifically exempt by law.

For property tax purposes, there are two broad ***classes of property***, real and personal. ***Real property*** consists of land and buildings, structures, or improvements that are affixed to the land. The Constitution requires that real estate (real property) constitute a single class. This requirement is significant in conjunction with the additional constitutional requirement that taxes be uniform within a class of property.

In general, everything else is referred to as ***personal property***. Because the Legislature has exempted motor vehicles, household goods, and personal effects, only that personal property used in business is now taxable.

In 1998, 92 percent of all assessed property subject to property tax was real property while only 8 percent was personal property. Nearly all of the taxable personal property belongs to businesses and consists primarily of machinery and equipment. Chart 3 displays the distribution of all taxable property, real and personal.

Chart 3
Distribution of Taxable Property - CY 1998



What are the Major Exemptions From Property Tax?

There are numerous other exemptions from property tax, established either by stature or constitutionally. Chart 4 lists the major exemptions from property tax and the savings to taxpayers from these exemptions in 1997-99.

Any property tax exemption has the effect of slightly increasing the tax rate that owners of all other taxable property must pay by reducing the overall base of taxable property. This circumstance of causing one segment of taxpayers' taxes to increase as a result of exempting the value of property of another segment of taxpayers is commonly referred to as a ***"tax shift**."*

As can be seen from Chart 4, these exemptions totaled $21 billion for 1998 in state and local tax savings. That is, *if* the exempt property were taxed at existing rates, these taxpayers would pay $21 billion more and all other taxpayers would pay $21 billion less.

The text of the original State Constitution declares, "Such property as the legislature may by general laws provide shall be exempt." It is this provision of the Constitution that allows the Legislature to grant property tax exemptions. Note that it allows the Legislature to exempt types of *property*; it does not allow the Legislature to exempt property based on its *owner*.

Chart 4
Major Exemptions from Property Tax - 1997-99 Biennium

Exemption	State Taxes	Local Taxes	Total
Intangible Property (e.g.. Cash, deposits, loans, securities)	3,342,463,000	11,183,410,000	14,525,873,000
Business Inventories	162,520,000	543,522,000	706,042,000
Household goods/personal effects	108,897,000	364,314,000	473,211,000
Senior Citizens	34,990,000	164,314,000	199,304,000
Churches	31,083,000	104,002,000	135,085,000
Nonprofit hospitals	23,293,000	77,934,000	101,227,000
Private schools and colleges	20,834,000	69,706,000	90,540,000
Agricultural products	13,491,000	45,118,000	58,609,000
All others	974,490,000	3,405,027,000	4,379,517,000
TOTAL	4,712,061,000	15,957,347,000	20,669,408,000

By far the largest exemption is that for intangible property. Exempt intangibles previously included money, mortgages, notes, accounts, stocks and shares of corporations, and other similar property. In 1997, the exemption for intangible property was significantly expanded to include trademarks, trade names, patents, copyrights, trade secrets, franchise agreements, licenses, etc.

When Were These Exemptions Granted?

The exemption for intangible property was originally granted by the Legislature in 1925 and has been amended several times, most recently in 1997. The exemption for business inventories was passed by the Legislature and phased in over ten years, beginning in 1974. Motor vehicles were exempted from property tax in 1937, when the current motor vehicle excise tax was enacted. As early as 1871, there were exemptions for household and personal effects, but the expanded exemption that individuals have today was granted in 1935. Churches and hospitals have exemptions that were granted prior to statehood, in 1854 and 1886 respectively. Computer software was exempted in 1991. Exemptions for agricultural products were subject to legislative changes from 1973 through 1984 when the current exemption for all such products was enacted. Private schools and colleges were exempted by the Legislature in 1925.

Note that each of these exemptions was granted in statute by the Legislature; only the exemption for senior citizens was authorized through a constitutional amendment.

What Types of Property Tax Relief are Available to Senior Citizens?

Senior citizen property tax exemptions originated with a constitutional amendment in 1966 and have been modified by the Legislature many times since. A constitutional amendment was required because senior citizen exemptions are based on the owner of the property not on the type of property.

Only low-income homeowners who are seniors (or are retired as a result of a physical disability) are eligible for property tax relief. This relief can come in the form of an exemption, a freeze in their assessed value, and/or a deferral of tax due, depending on individual circumstances.

Homeowners 61 years of age and older may apply for an exemption from paying excess levies if their household income is $30,000 or less. The property tax relief is available for taxes payable in the year after the application is made and every year thereafter. They are also exempt from regular levies on a portion of their home value if their income is $24,000 or less.[1]

1 A further benefit for these homeowners with incomes of $30,000 or less is that the taxable value of the property is frozen when the homeowner becomes eligible for the program.

A related program allows homeowners at least 60 years of age with household incomes of $34,000 or less to defer payment of all property taxes. These taxes may be deferred until the sale of the property or until the property ceases to be the permanent residence of the homeowner or surviving spouse.

While property tax exemptions are quite popular with low-income seniors, deferrals apparently are not. Even though the eligibility requirements are broader for the deferral program than for the exemptions, only 1,400 people took advantage of the available tax deferral for 1998, compared to 132,000 receiving exemptions.

What are "Current Use" Valuations and "Open Space?"

Although not a tax exemption in a strict sense of the term, ***current use valuations*** reduce the tax burden on certain properties and in doing so "shift" taxes to other taxpayers just as an exemption does. This is done by allowing the assessed value to be determined based on the use which the property is currently utilized rather than the market value (or the "highest and best use") of the property. Establishment of the current use programs required a constitutional amendment, passed by the voters in 1969, to create an exception to the constitutional requirement that all real property be treated uniformly. The amendment allowed the 1970 Legislature to create a program for current use valuation that was further expanded in 1973.

The program allows agricultural lands, timberlands, and other "open space" lands to be assessed according to their value as they are currently being used, rather than the market value. This "current use" value is typically much lower than market value and is therefore a tax benefit for the property owner. ***"Open space"*** lands are lands which conserve natural resources, promote conservation, enhance public value and recreation, preserve visual quality, or have other legislatively identified attributes which are of public benefit. Agricultural and timber lands are subject to various requirements regarding size, use, and income. When property is removed from the current use valuation program, either by the owner or the assessor due to a change in use, back taxes must be paid.

What Types of Restrictions and Limitations are There on Property Tax Collections?

The myriad of constitutional and statutory provisions regarding property taxes has served to create an interconnected system of property tax administration and collection. In order to understand the overall system and the rationale for its evolution, it is important to review the restrictions and limitations governing property taxes.

Uniformity in Taxation

Perhaps the most important principle of property taxation in our state is the uniformity of taxation. In the 1853 Organic Act establishing the government of the Washington Territory, the U.S. Congress imposed a strong requirement for uniformity in taxation in order to prevent the territory's residents from imposing a disproportionate share of taxes on nonresidents. Uniformity of taxation continued as a fundamental principle in the State Constitution adopted in 1889.

The State Constitution includes a ***uniformity clause***, adopted in 1931, that provides "taxes shall be uniform upon the same class of property within the territorial limits of the authority levying the tax... All real estate shall constitute one class." This means that taxes must be the same on real property of the same market value. Uniformity requires both an equal rate of tax and equality in valuing the property taxed. Many other states have differential tax rates or different value standards that depend upon the separate classifications of property. Such a system would not be constitutional in Washington.

One Percent Limit

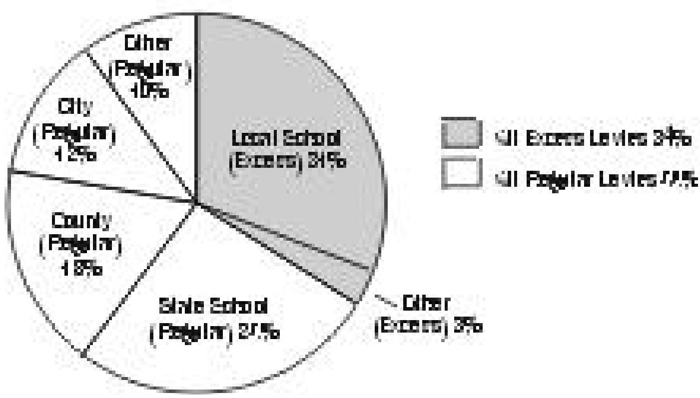
Beyond the principle of uniformity, the Washington State property tax system as we know it today really took shape in the early 1970s. In 1972, Washington State voters amended the Constitution to limit the annual amount of property taxes that may be imposed on an individual parcel of property to 1 percent of its true and fair value, or $10 per $1,000 of value. Under the constitutional amendment, the ***1 percent limit*** may be exceeded only with the approval of 60 percent of the district's voters.

Taxes imposed under the 1 percent limit are termed ***"regular" levies***, while those outside the limit are ***"excess"*** or ***"special" levies***. For statewide taxes due in 1998, 66 percent are regular levies and 34 percent are excess voter-approved levies. The majority of excess levies are school district levies. Chart 5 breaks down the statewide average regular and excess levies by type of taxing district.

The 1 percent maximum rate for regular property taxes is limited further by a complex series of statutes. By law, tax rates are stated in terms of dollars per $1,000 of value. Therefore, the 1 percent limit is the same as $10 per $1,000. The $10 limit is broken down as follows: $3.60 is reserved for the state with $0.50 available for four additional purposes: preservation of open space, emergency medical services, affordable housing, or metropolitan parks in larger cities.

The remaining $5.90 is available to local districts. Counties, cities, and road districts are known as "senior districts" and get first priority in levying the $5.90. Counties are allocated $1.80 and cities receive $3.60 (or less if library or fire protection services are provided by separate districts rather than the city). In unincorporated areas, there is no city levy but a county road levy of $2.25 is authorized.

Chart5
Breakdown of Regular and Excess Levies - CY 1998



The remaining portion of the $5.90 is allocated to ***"junior" districts,*** which include fire districts, water districts, park and recreation districts, cemetery districts, hospital districts, stadium districts, flood control districts, airport districts, and numerous others. Even though each junior district also has a statutory limit on its tax rate, the cumulative total of the allowable rate limits for all senior and junior districts exceeds the $5.90 limit. In the event the cumulative rates levied on a parcel of property by all of the districts might actually exceed $5.90 per 1,000, the rates are prorated down until they reach $5.90. Senior districts get priority over junior districts in this process.

The state portion of the property tax is often referred to as the state school levy, because the statutes designate the $3.60 maximum state levy be used solely for support of public schools.

The "old" 106 Percent Limit and the "new" Limit Factor

Subject to constitutional and statutory limits, local government taxing districts generally determine their property tax levy based on the revenue required to fund their budget for the following year. Perhaps the most significant limitation to that practice was the creation of the 106 percent limit. In 1971, the Legislature imposed a statutory limit on annual increases in local governments' revenues from property taxes. The 1979 Legislature extended this limit to the state property tax as well.

Under the old *106 percent limit*, revenues from any district's *regular* property tax levy may not exceed 106 percent of the highest amount of revenue received from any levy in the preceding three years. Added to this is an amount to account new construction and improvements.

In 1997, voters passed Referendum 47 (described fully on page 18), which changed the workings of the 106 percent limit. Now, a taxing district is only allowed to increase its levy by the lesser of inflation or 6 percent. Taxing districts are no longer allowed to increase automatically by 6 percent each year. For a district to increase the levy by the full 6%, a super majority vote of the governing body in each district is required. For taxes due in 1998 this inflation limit factor was 1.9 percent and in 1999 is projected to be 0.85 percent. Taxing districts with fewer than 10,000 residents can still use the full 6 percent without a supermajority vote.

The limit factor (or inflation factor) applies only to regular levies and not to excess levies. It restricts generally the total amount of property tax revenue that any district can raise in a given year and therefore tends to limit taxes. ***Importantly: It does not necessarily restrict the amount of increased taxes on an individual property, nor does it limit the amount of increase in the assessed value of a particular property.*** It can affect individual property owners quite differently. Taxpayers with larger than average assessed value increases will often see tax increases in excess of the limit factor. Those with assessed values that grow slowly or not at all will see tax increases less than the limit factor. Again, the limit factor simply controls the total tax collections within a district not necessarily the taxes paid by each taxpayer.

How are Individual Property Taxes Determined?

The tax on a particular property is calculated by multiplying its assessed value by the tax rate. Once the maximum allowable regular property tax levy amount is determined for a district under the limit factor, the county assessor then calculates the necessary tax rate by dividing the total levy amount by the amount of taxable property (total assessed value) in the district. The rate is expressed in terms of dollars per $1,000 of valuation. The rate is multiplied by each $1,000 in value for each parcel to determine the tax. An individual tax bill is the sum total of all such calculations for all of the individual districts levying tax on the particular property.

The Constitution stipulates that property tax is to be levied against the "true and fair" value of property. Property assessment, or ***valuation***, is the process by which the "true and fair" value is determined. In order to comply with the provisions of the Constitution, all taxable property must be assessed at 100 percent of its true and fair value unless the law specifically provides otherwise, such as with low-income senior citizens. A county assessor makes these assessments for about 97 percent of the property in the state. The Department of Revenue makes the remaining 3 percent of the assessments.

How is Property Assessed and the Tax Collected?

All property except new construction is assessed on its value as of January 1 of the assessment year and is listed on the tax rolls by May 31. For new construction, the July 31 value is listed. Notices of valuation changes are mailed to the owner of the property. Taxpayer appeals of assessed values must be filed with the county Board of Equalization by July 1 or 30 days following the mailing of the notice of revaluation, whichever is later. However, the county legislative authority may authorize up to 60 days.

The treasurer in the county where the property is located collects property taxes. The treasurer is required to send each taxpayer a notice which must include the amount of tax owed, the value of both real and personal property, and the name and amount for each taxing district levying a tax. The notice must also separately state the amount of excess (voter-approved) levies. The county treasurer mails the tax bill to the "taxpayer" listed on the tax rolls, which may be a lending institution in cases where the property owner has provided that taxes are to be paid from a reserve account administered by the lending institution. The treasurers mail tax bills after February 15. The first half of the tax is due by April 30; the second half by October 31. Given the timelines required for revaluation and billing, the taxes due in any particular year are based upon the assessed value from the preceding year.

There are three criteria used by assessors in valuing real property: ***comparable sales, cost***, and ***income potential***. Statutes require that determination of the true and fair value of the property be based on the sales of comparable property, provided those sales are representative of the market demand, or *market value*, for such property. In addition to comparable sales, assessors may also consider the cost or replacement cost of the real property. A third criterion that may be considered is the income potential that "would be derived from prudent use of the property." The cost and income criteria may be the dominant factors in determining property value only when there are not sufficient comparable sales, for "property of a complex nature," or for a public utility. One, two or all three criteria may be applied to a given parcel.

For many years, assessment practices varied widely across the state, resulting in both constitutional and statutory changes intended to improve adherence to requirements for uniformity. In the early 1950s, with the imposition of the real estate excise tax, the state began to receive accurate data on actual sales prices of real property which revealed significant inequities between the assessed value and the actual market value among taxpayers living in different areas of the state. In 1955, the Legislature required that no property go more than four years without its value being reassessed.

More frequent revaluation of property improves uniformity when market values are increasing because property assessments more closely reflect the current value. Otherwise, some property is valued based on current values while other property valuations lag far behind the market value. Decreasing the amount of time between revaluations also lessens the amount of each increase in value. Of the 39 counties today, 20 revalue on a four-year cycle and 17 revalue annually, with only two counties on two or three year cycles. Since several counties with large property bases revalue annually, the large majority of property in the state is revalued annually.

What Does Equalization of Assessments Mean?

Still, differences do exist in revaluation cycles and assessment practices among counties. Recall that the Constitution requires taxes on real estate to be uniform within a district and that for the purpose of collecting the state property tax, the state is one district. Since differences in county assessment practices would result in the state property tax being applied non-uniformly across the state, it is necessary for the state Department of Revenue to estimate the relationship in each county between the assessed value and the actual market value. This relationship is stated in terms of a ratio called the "***indicated ratio***." The estimates are done on the basis of averages determined from sampling individual parcels.

For the 1998 assessment year, the "indicated ratio" of assessed value to market value ranged from 0.995 (very close to a actual value) in Island County to 0.75 in Pend Oreille (75 percent of actual value). The statewide average indicated ratio for all counties was 0.90. The Department of Revenue does *not* then adjust assessed values for each property in a given county, but it does adjust the state property tax rate according to the indicated ratio for that county. The effective state property tax rate is therefore different in each county, but this rate multiplied by the assessed value results in a uniform tax across the taxing district, which is the entire state. This process is called "***equalization***."

Are Public Schools Funded from the Property Tax?

The Washington State Constitution established basic education as the state's paramount duty. Subsequent statutes and court decisions have established that the *state* must provide sufficient aid to local school districts to fund basic education. As a result, spending for public schools accounts for almost one-half of the state General Fund budget.

As mentioned earlier, the state property tax levy is dedicated for public schools and is frequently termed the state school levy. The revenues are paid directly into the General Fund, along with all the other tax revenues that go to the General Fund. They are not placed in a separate public school account.

The revenue from the state school levy is equal only to about one quarter of the General Fund allocation to public schools from the state budget. Revenue from the state property tax levy, $2.5 billion for the 1997-99 biennium, is deposited into the state General Fund. The General Fund also receives $15.2 billion from sales tax, business and occupation tax, real estate excise tax, and the other revenue sources shown on Chart 1. Although the state will collect only $2.5 billion in property taxes specifically dedicated for schools, the state appropriated $8.3 billion public schools from the General Fund for the same two-year period.

The state school levy as we know it today was enacted in 1975. Prior to 1975, property owners paid a *local regular* school levy of $3.60 per $1,000. At that time, the state also funded more than half of statewide school operating budgets from general revenues. State aid was "equalized" in an effort to offset the differences in per student tax revenues between school districts that resulted from the local regular school levy. Those differences occurred because districts with greater total property value relative to their number of students were able to generate more revenue per student from the same tax rate than was a district with low property value. School districts also had the ability to collect excess property tax levies, subject to voter approval.

In 1975, the local regular levy was replaced by the regular state levy and state aid was increased to replace the lost local revenue. Over the following few years, the state moved rapidly to full funding of basic education from the state General Fund.

Today, local school districts are allowed to collect excess property tax revenues, with voter approval, to enrich their programs beyond the level of basic education. These local school excess levies are limited to an amount equal to 24 percent of revenues received from state and federal sources. Certain districts that were collecting a higher percentage of property taxes before the "*levy lid*" was imposed are still able to collect an amount greater than 24 percent through a "grandfather clause" in the statute. Excess school levies for maintenance and operations may be for a period of up to four years and require a 60 percent voter approval. Subject to similar voter approval requirements, districts may also levy property taxes to fund school construction, technology and school buses.

As illustrated on Chart 2, school district excess levies account for 32 percent of the total property taxes collected statewide. The state property tax levy (also dedicated for schools) accounts for another 26 percent.

How do Washington State Property Taxes Compare?

This section examines a number of comparative statistics regarding property taxes in Washington State, including comparisons with other states and historical comparisons to examine how property taxes have changed over time. The analysis is accomplished largely through the use of a series of graphic presentations.

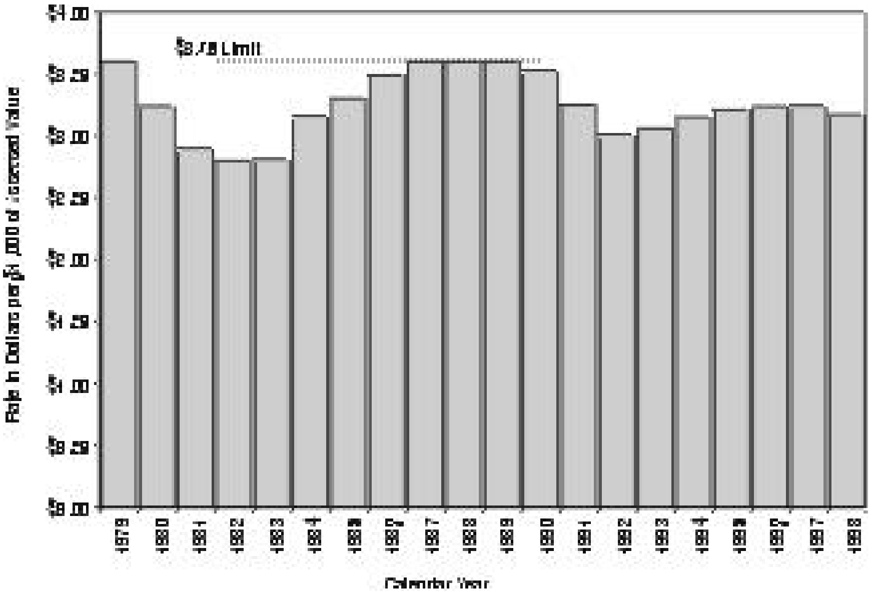


Chart 6 shows the history of the state property tax rate. The rate is statutorily limited to $3.60 per $1,000 of assessed value, however it does fluctuate from year to year due to the interaction between property values and levy limitations. The rate in 1998 was only $3.17.

Chart 7
Comparison of Washington Property Taxes to Other States - CY 1998

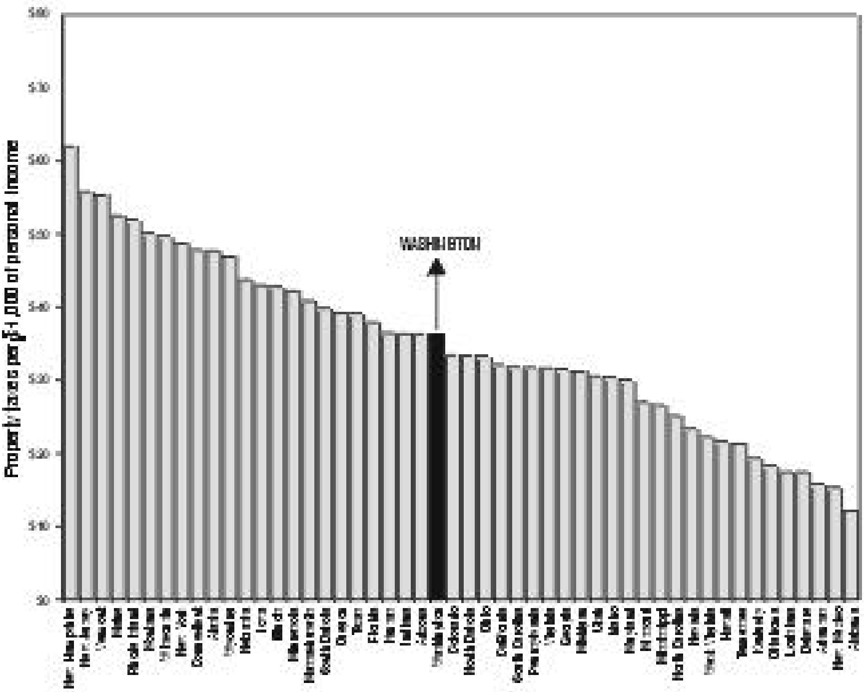
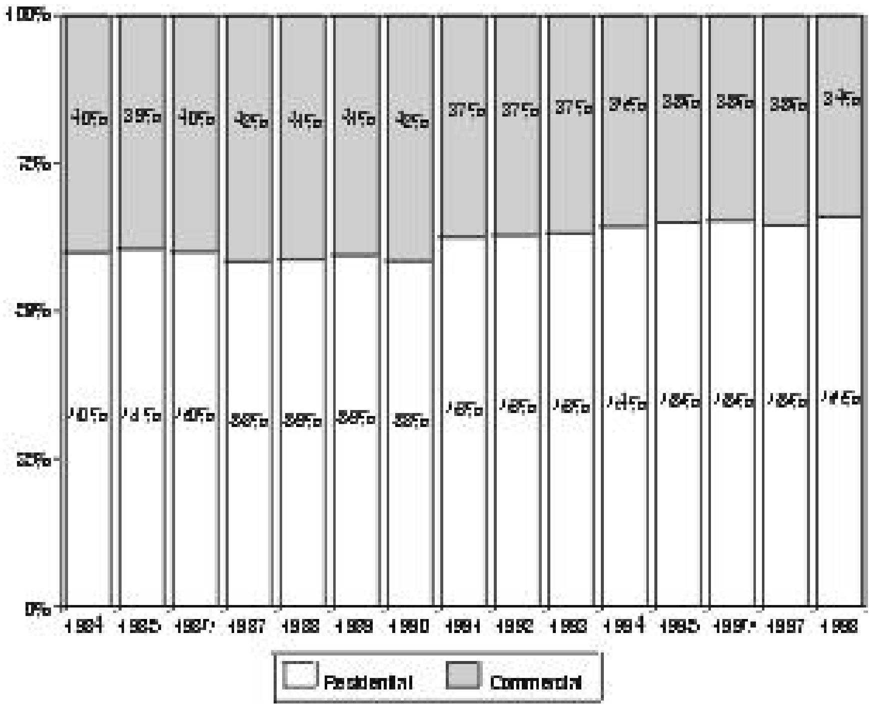


Chart 7 is a comparison among all states of property taxes relative to income. When compared to the other 49 states, state and local property taxes in Washington appear to be about in the middle. For taxes due in 1995, Washington ranked 24th in property taxes at $36.30 per $1,000 of personal income. Washington property taxes were just slightly above the national average of $36.02. Calculated on a per capita basis, Washington ranked 18th at $805 per person.

A recent trend, particularly since the early 1990s, has been the shift of the tax burden from taxpayers whose property is not increasing in value to taxpayers whose property is increasing in value. The real estate boom in King County of the early nineties was primarily a *residential* real estate boom. Commercial properties were generally not increasing at the rate of residential properties. As can be seen from Chart 8, the proportions of statewide assessed value (and therefore the tax burden) of commercial and residential property have been changing.

Chart 8
Relative Residential/Commercial Property Tax Burden



In 1990, commercial property represented 42 percent of the statewide assessed value, and therefore paid 42 percent of the property taxes. Since then, the relative share of commercial assessed value (and therefore taxes) has decreased by 8 percent points to 34 percent.

What are Some of the Recent Legislative Changes to the Property Tax?

Referendum 47 (SB 5835 - Chapter 3, Laws of 1997)

In an attempt to address many of the perceived problems within the property tax system, the legislature passed SB 5835 that was placed on the ballot as Referendum 47. In November 1997, the voters passed the referendum that included three major components; a permanent reduction in the state property tax, a change to the 106% limit, and value averaging to prevent large valuation increases. The state supreme court later ruled this last component to be unconstitutional.

106 Percent Limit. The 106 percent limit is changed to the lesser of (1) 106 percent or (2) "the limit factor," which is defined as 100 percent plus the percentage change in the implicit price deflator for personal consumption (inflation). However, the old 106 percent limit still applies to taxing districts with populations less than 10,000. In addition all taxing districts may exceed the limit factor with a two-thirds vote of the relevant governing body.

Reduction in the state levy. The state property tax levy was reduced by 4.7%. This has the effect of reducing all future state levies. (In addition, the state levy is now calculated based upon the inflation-based limit factor rather than the 106% limit. This further reduces the state property tax.)

Value Averaging. A limitation is placed on adding large valuation increases. Each year, the current appraised value is compared to the assessed value for the previous year and any increases in valuation (in most cases) are limited to 15% per year. With such a limitation, the assessed value would return to market value within a few years even in heated real estate markets.

On July 30, 1998, the state Supreme Court in Belas v. Kiga invalidated the value averaging provisions of Referendum 47. In invalidating the value-averaging provisions, the court stated that Referendum 47 intentionally creates a different assessment ratio for property which is appreciating at a rate in excess of 15 percent than it does for property which is not appreciating as rapidly. This difference in assessment ratio causes a lack of uniformity in the tax burden. The court held that this scheme violated the uniformity requirement of the Constitution because all real property is one class for tax purposes.

Exemption for Intangibles (ESSB 5286 - Chapter 181, Laws of 1997)

ESSB 5286 expanded the exemption for intangible personal property to include ALL intangible property. Intangible property exempt from tax now includes all items previously exempt plus items such as trademarks, trade names, brand names, patents, copyrights, trade secrets, franchise agreements, licenses, permits, core deposits of financial institutions, noncompete agreements, clientele, customer lists, patient lists, favorable contracts, favorable financing agreements, reputation, exceptional management, prestige, good name, or integrity of a business. The exemption does not include characteristics or attributes of property such as zoning, location, view, geographic features, easements, covenants, proximity to raw materials, condition of surrounding property, proximity to markets, and the availability of a skilled work force.

Senior Citizen Exemption Program (ESSB 6533 - Chapter 333, Laws of 1998)

Participation in the senior citizen program was expanded and the amount of tax benefit was increased in ESSB 5835. The income levels for determining eligibility in the program were increased. The top category now includes those with incomes up to $30,000 (was $28,000). The middle category now covers incomes from $18,000 to $24,000 (was $15,000 to $18,000) and the lowest category covers seniors with incomes up to $18,000 (was $15,000.) In addition, the maximum income for valuation freeze eligibility was increased to $30,000 (was $28,000). Finally, the amount of tax relief given to taxpayers eligible under the first two categories (up to $24,000) was increased.

What Legislative Changes to the Property Tax might be proposed in the future?

Multiple Classification Systems ("Split Rolls")

In many states, property tax classification systems provide for different classes of property which are subject to different tax rates or valuations. For example, residential property might be classified separately from commercial property and taxed at a lower rate. Different types of commercial property might be separated into classes and taxed at different rates, much the same as our state administers the business and occupation tax. To do so will likely require a constitutional amendment due to the provisions of the uniformity clause. Whenever the value of one type of property is reduced (either through split rolls or exemptions), taxes are shifted to other taxpayers and some taxing districts may receive less revenue.

Homestead Exemptions and Credits

Homestead exemptions and credits apply specifically to owner-occupied residential property. Homestead *exemptions* reduce the assessed value of a homeowner's property. For example, a homeowner might be exempt from paying tax on the first $50,000 in value on the home; or perhaps a homeowner's primary residence is exempt from property tax altogether. That tax burden is shifted to property owners who don't get the homestead exemption, such as homeowners with higher-valued property or commercial property owners. Again it is likely that such a proposal would require a constitutional amendment.

Alternatively, homestead *credits* are amounts subtracted from the tax owed. The assessed value and taxes are calculated as with all other property, but then the homeowner receives a tax credit that decreases the actual tax bill. As a result, taxing districts (including the state) lose revenue but there is no shift of the taxes to other taxpayers.

Thirty-seven states offer homestead exemptions or credits; 14 states and the District of Columbia have programs with no age limits; 14 states have programs for seniors only; and nine states offer programs for all ages with more generous benefits for senior citizens.

Tax Deferrals

Sixteen states and the District of Columbia offer deferral programs that allow certain people, usually the elderly and disabled, to postpone paying property taxes until death or the sale of their property. The programs in 14 states (including Washington) are limited to persons over a certain age.

Legislation has been introduced to expand options for tax deferrals to other taxpayers in our state. Legislation has been proposed to allow deferral of taxes for low-income homeowners of any age and to allow deferral of tax increases beyond a certain percentage, regardless of age or income. Such proposals are intended to lessen the possibility that taxpayers will lose their homes because of rising taxes.

Other taxpayers are unaffected because tax deferrals do not shift taxes to other taxpayers. Since the program is a deferral and not an exemption, the taxes are recovered over time.

Administrative Changes

Numerous bills have been introduced that would change the way the property tax is administered. Bills have been introduced to provide additional information on revaluation notices and tax statements, to have tax statements sent to the property owner as well as the person paying the tax, to prohibit further increases in valuation during administrative appeals, and to require cities to notify assessors when action they take could affect land values.

Bills have also been introduced to eliminate the hardship of paying taxes twice a year. These bills have authorized quarterly or monthly payments. Legislation has been considered to require annual revaluation of all property in order to decrease the magnitude of any one increase in assessed value. For counties on revaluation cycles longer than two years, the change in value for an individual parcel of property follows a stair-step pattern. For example, in a four-year revaluation cycle, there is no change in value for a parcel of property for three years. In the fourth year, there could be a substantial change in value representing four years of value growth.

Conversely, some people like the three-year "free ride" under the four-year cycle. Annual revaluations also require a greater commitment of resources at the county level, and the change in valuation in some counties may be so gradual as not to justify annual revaluations.

Glossary

Class of Property: The term is used in the State Constitution to describe a broad type of property. There are only two classes of property— real property (real estate) and personal property (everything else).

Comparable Sales Approach: A criterion which assessors use in determining the value of a parcel of property. In fact, it is the primary criterion that assessors are required to use in determining value. Assessors look at the dollar value of sales of comparable parcels of property.

Cost Approach: Cost (or replacement cost) is a criterion which assessors may use in determining the value of a parcel of property. In the absence of definitive data on comparable sales, assessors examine the cost, or replacement cost, of the parcel of property.

Current Use Valuation: A method of establishing the assessed value of a parcel of property which allows the assessor to determine value based on the use for which the property is currently utilized rather than the market value. Current use valuation allows an owner to reduce the tax burden on agricultural lands, timberlands, and open space lands. For example, agricultural lands may be valued based on their production, even though the property has a higher market value as commercial property or a housing development.

Equalization: A process by which the state Department of Revenue adjusts the state property tax rate within each county to account for differences in assessment practices between the 39 counties in which the state property tax is levied. Equalization is necessary to ensure that the state property tax is levied uniformly on taxpayers across the state.

Excess (or Special) Levy: Property taxes imposed in excess of the 1 percent constitutional limit which must be voter approved.

Income Approach: Income is a criterion which assessors may use in determining the value of a parcel of property. In the absence of definitive data on comparable sales, assessors estimate the income potential of a parcel of property and its effect on market value.

Indicated Ratio: The statistical ratio between the average assessed value of property within a county and the actual market value of property within the county. The indicated ratio for each county is determined by the state Department of Revenue on the basis of averages derived from sampling individual parcels within the county. Indicated ratios are used in equalizing the state property tax levy across the state to ensure uniform taxation.

Junior Districts: Taxing districts which can levy property taxes but which have a lower priority in levying property taxes than counties, cities, and road districts. Junior districts include fire districts, library districts, water districts, park and recreation districts, hospital districts, cemetery districts, flood control districts, and numerous others.

Limit factor: A statutory limit approved by the voters in Referendum 47 defined as 100 percent plus the percentage change in the implicit price deflator for personal consumption (inflation).

One Percent Limit: A constitutional provision limiting the annual amount of property taxes that may be imposed on an individual parcel of property, without voter approval, to 1 percent of its true and fair value.

Open Space: Open space lands are lands which conserve natural resources, promote conservation, enhance public value and recreation, preserve visual quality, or have other attributes which are of public value. Such lands are eligible for valuation based on current use rather than market value.

Personal Property: All property, tangible and intangible, which is not real property (real estate) is personal property.

Real Property: Real property consists of land and the buildings, structures, or improvements that are affixed to the land. Real property and real estate are use synonymously.

Regular Levy: Property taxes imposed under the constitutional 1 percent limit on levies are termed regular levies. Regular levies do not require voter approval.

Split Roll: Taxing one type of property differently than another type. The example most often cited is taxing commercial property differently than residential property.

Tax Shift: Causing one segment of taxpayers' taxes to increase as a result of exempting the value of property of another segment of taxpayers. For example, exempting a portion of residential property may cause taxes on commercial property to increase.

Uniformity Clause: Article 7, Section 1 of the State Constitution requires "All taxes shall be uniform upon the same class of property within the territorial limits of the authority levying the tax..." Uniformity requires both an equal rate of tax and equality in valuing the property to be taxed. The Constitution also stipulates that real estate is one class of property.

Valuation: The process used by the assessor to determine the true and fair value, or the assessed value, of property. Another term for valuation is property assessment.

106 Percent Limit: A statutory limit imposed by the Legislature in 1971 (in 1979 for the state levy) that limits annual increases in property tax revenues for a taxing district from regular levies to no more than 106 percent of the highest amount of revenue from any levy in the past three years. (see also ***Limit Factor*** above)

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